

BANKRUPTCY AND BUSINESS FAILURES IN THE UNITED STATES, 1980-1983:

A BRIEF SURVEY OF DEVELOPMENTS

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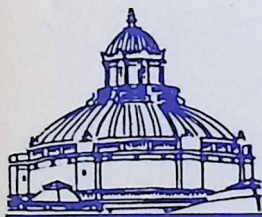
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September 30, 1983

HG 3760

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ABSTRACT

This report presents bankruptcy and business failure statistics from 1973 to 1983 and reviews various studies which assess the causes for the sharp rise in bankruptcy filings after passage of the Bankruptcy Reform Act in 1979. It also describes major events in corporate bankruptcy since 1980 and some of the legislative steps relating to bankruptcy taken by the 98th Congress.

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Abstract

This report presents a summary of the results of a study conducted in 1987 and 1988. The study was designed to investigate the effects of a new teaching method on student learning. The results of the study are presented in the following sections. The first section describes the study design and the second section presents the results of the study. The third section discusses the implications of the results and the fourth section presents the conclusions of the study.

1. Introduction

2. Method

3. Results

4. Discussion

5. Conclusion

6. References

7. Appendix

8. Glossary

9. Index

10. Acknowledgments

11. About the Author

12. Contact Information

13. Copyright Notice

14. Disclaimer

15. Privacy Policy

ACKNOWLEDGEMENTS

The author wishes to express his deep appreciation to Mark Jickling for his statistical and library assistance at all stages of the preparation of this report; to Kevin Winch, Edward Knight, Jean Wells, William Jackson, David Whiteman, and Robert Ujevich for their helpful criticism of preliminary drafts of the study; and to John Colletta and John Williamson for the preparation of the final draft.

MEMORANDUM

The following is a summary of the information received from the various sources mentioned in the report. It is to be understood that this summary is not intended to be a complete statement of the facts, but rather a statement of the information received from the sources mentioned. The information is being furnished for your information and for the use of the various departments of the Government.

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CONTENTS

ABSTRACT	iii
ACKNOWLEDGEMENTS	iv
SUMMARY AND CONCLUSION	vii
INTRODUCTION	1
I. BANKRUPTCY AND BUSINESS FAILURE TRENDS, 1973-1983	3
Table 1. Bankruptcy Filings and Business Failures, by Quarter, 1973-1983	5
Chart 1. Bankruptcies and Business Failures by Quarter, 1973-1983	7
Table 2. Bankruptcy Class Filed, by Chapter of the Bankruptcy Code, October 1979-June 1983	9
Chart 2. Personal Bankruptcy Filings in the United States by Chapter of the Bankruptcy Code, Years Ending June 30, 1971-1982	10
II. STUDIES RELATING TO THE IMPACT OF THE BANKRUPTCY REFORM ACT	15
III. DEVELOPMENTS IN CORPORATE BANKRUPTCY	25
A. Chapter 11 Filings by Asbestors Companies	26
B. Chapter 11 Filings because of Wage Costs	29
C. Other Large Corporate Bankruptcies	31
IV. LEGISLATIVE INITIATIVES ON BANKRUPTCY ISSUES	33

CONTENTS

1	INTRODUCTION	1
2	THE PROBLEM OF THE PROBLEM	2
3	THE PROBLEM OF THE PROBLEM	3
4	THE PROBLEM OF THE PROBLEM	4
5	THE PROBLEM OF THE PROBLEM	5
6	THE PROBLEM OF THE PROBLEM	6
7	THE PROBLEM OF THE PROBLEM	7
8	THE PROBLEM OF THE PROBLEM	8
9	THE PROBLEM OF THE PROBLEM	9
10	THE PROBLEM OF THE PROBLEM	10
11	THE PROBLEM OF THE PROBLEM	11
12	THE PROBLEM OF THE PROBLEM	12
13	THE PROBLEM OF THE PROBLEM	13
14	THE PROBLEM OF THE PROBLEM	14
15	THE PROBLEM OF THE PROBLEM	15
16	THE PROBLEM OF THE PROBLEM	16
17	THE PROBLEM OF THE PROBLEM	17
18	THE PROBLEM OF THE PROBLEM	18
19	THE PROBLEM OF THE PROBLEM	19
20	THE PROBLEM OF THE PROBLEM	20
21	THE PROBLEM OF THE PROBLEM	21
22	THE PROBLEM OF THE PROBLEM	22
23	THE PROBLEM OF THE PROBLEM	23
24	THE PROBLEM OF THE PROBLEM	24
25	THE PROBLEM OF THE PROBLEM	25
26	THE PROBLEM OF THE PROBLEM	26
27	THE PROBLEM OF THE PROBLEM	27
28	THE PROBLEM OF THE PROBLEM	28
29	THE PROBLEM OF THE PROBLEM	29
30	THE PROBLEM OF THE PROBLEM	30
31	THE PROBLEM OF THE PROBLEM	31
32	THE PROBLEM OF THE PROBLEM	32
33	THE PROBLEM OF THE PROBLEM	33
34	THE PROBLEM OF THE PROBLEM	34
35	THE PROBLEM OF THE PROBLEM	35
36	THE PROBLEM OF THE PROBLEM	36
37	THE PROBLEM OF THE PROBLEM	37
38	THE PROBLEM OF THE PROBLEM	38
39	THE PROBLEM OF THE PROBLEM	39
40	THE PROBLEM OF THE PROBLEM	40
41	THE PROBLEM OF THE PROBLEM	41
42	THE PROBLEM OF THE PROBLEM	42
43	THE PROBLEM OF THE PROBLEM	43
44	THE PROBLEM OF THE PROBLEM	44
45	THE PROBLEM OF THE PROBLEM	45
46	THE PROBLEM OF THE PROBLEM	46
47	THE PROBLEM OF THE PROBLEM	47
48	THE PROBLEM OF THE PROBLEM	48
49	THE PROBLEM OF THE PROBLEM	49
50	THE PROBLEM OF THE PROBLEM	50
51	THE PROBLEM OF THE PROBLEM	51
52	THE PROBLEM OF THE PROBLEM	52
53	THE PROBLEM OF THE PROBLEM	53
54	THE PROBLEM OF THE PROBLEM	54
55	THE PROBLEM OF THE PROBLEM	55
56	THE PROBLEM OF THE PROBLEM	56
57	THE PROBLEM OF THE PROBLEM	57
58	THE PROBLEM OF THE PROBLEM	58
59	THE PROBLEM OF THE PROBLEM	59
60	THE PROBLEM OF THE PROBLEM	60
61	THE PROBLEM OF THE PROBLEM	61
62	THE PROBLEM OF THE PROBLEM	62
63	THE PROBLEM OF THE PROBLEM	63
64	THE PROBLEM OF THE PROBLEM	64
65	THE PROBLEM OF THE PROBLEM	65
66	THE PROBLEM OF THE PROBLEM	66
67	THE PROBLEM OF THE PROBLEM	67
68	THE PROBLEM OF THE PROBLEM	68
69	THE PROBLEM OF THE PROBLEM	69
70	THE PROBLEM OF THE PROBLEM	70
71	THE PROBLEM OF THE PROBLEM	71
72	THE PROBLEM OF THE PROBLEM	72
73	THE PROBLEM OF THE PROBLEM	73
74	THE PROBLEM OF THE PROBLEM	74
75	THE PROBLEM OF THE PROBLEM	75
76	THE PROBLEM OF THE PROBLEM	76
77	THE PROBLEM OF THE PROBLEM	77
78	THE PROBLEM OF THE PROBLEM	78
79	THE PROBLEM OF THE PROBLEM	79
80	THE PROBLEM OF THE PROBLEM	80
81	THE PROBLEM OF THE PROBLEM	81
82	THE PROBLEM OF THE PROBLEM	82
83	THE PROBLEM OF THE PROBLEM	83
84	THE PROBLEM OF THE PROBLEM	84
85	THE PROBLEM OF THE PROBLEM	85
86	THE PROBLEM OF THE PROBLEM	86
87	THE PROBLEM OF THE PROBLEM	87
88	THE PROBLEM OF THE PROBLEM	88
89	THE PROBLEM OF THE PROBLEM	89
90	THE PROBLEM OF THE PROBLEM	90
91	THE PROBLEM OF THE PROBLEM	91
92	THE PROBLEM OF THE PROBLEM	92
93	THE PROBLEM OF THE PROBLEM	93
94	THE PROBLEM OF THE PROBLEM	94
95	THE PROBLEM OF THE PROBLEM	95
96	THE PROBLEM OF THE PROBLEM	96
97	THE PROBLEM OF THE PROBLEM	97
98	THE PROBLEM OF THE PROBLEM	98
99	THE PROBLEM OF THE PROBLEM	99
100	THE PROBLEM OF THE PROBLEM	100

SUMMARY AND CONCLUSION

Since the Bankruptcy Reform Act went into effect in October 1979, less than four years ago, it has been the focus of substantial controversy and concern. Two major phenomena since that date have received particular attention. First is the sharp rise in bankruptcy filings, of which personal bankruptcies are numerically by far the largest part. Second is the resort to reorganization proceedings under Chapter 11 of the new Bankruptcy Code by corporations that are currently solvent but whose solvency is in jeopardy as a result of anticipated damage claims or actual labor contracts.

There is much disagreement as to the extent to which provisions of the Bankruptcy Reform Act are responsible for the rise in personal bankruptcy filings. The studies on this subject reviewed in this report reach conclusions ranging from those which attribute the increase primarily to the Act to those which view the impact of the Act as very small. A clear answer is made difficult for several reasons. The initial impact of the Act coincided to a great extent with economic factors which also contributed to the increase, notably the economic recession combined with a continuing increase in the availability and use of consumer credit. In addition, there are many intangible factors, such as the decreased stigma attached to declaring bankruptcy, the impact of advertising by lawyers seeking bankruptcy business, and greater public awareness among debtors of how the Act may be used to get a "fresh start."

The statistics which show a one-time sharp increase in personal bankruptcies in the first year the Act was in effect and a levelling off and

even some decline since then suggest, as some observers have noted, that the Act may have had a one-time impact changing the level of personal bankruptcy filings, but that it is unlikely to cause a further increase in the number of such filings.

It is too early to forecast the outcome of attempts of asbestos manufacturing companies, notably the Manville Corporation, to utilize the provisions of the Bankruptcy Code to forestall potentially ruinous lawsuits and of other firms to overturn the onerous terms of contracts with labor unions. These cases are still before the courts and substantial further judicial review can be anticipated.

Congressional interest in possible amendments to the Bankruptcy Reform Act has been concentrated on provisions affecting personal bankruptcy. One possible approach, backed by many firms in the consumer credit industry, is to make it more difficult for debtors to file for bankruptcy unless they agree to pay a reasonable portion of their debts from future income. Such a provision is considered unnecessary at this time by others who believe that there should be more experience under the Act before major amendments are adopted. Some persons opposing major revision do support more limited changes in the Act to deal with the cases of flagrant abuse which have occurred since 1979.

BANKRUPTCY AND BUSINESS FAILURES IN THE UNITED STATES, 1980-1983:

A BRIEF SURVEY OF DEVELOPMENTS

INTRODUCTION

The Bankruptcy Reform Act of 1978 (Public Law 95-598) is widely recognized as the most sweeping revision of the bankruptcy laws of the United States since 1938. Its impact may be substantial, but there is, as yet, little consensus as to precisely what that impact is likely to be. This is due, of course, in part to the fact that many provisions of the Act are still untested in the courts and that experience under the Act is still relatively limited.

Two trends that may well relate to the Act are evident. First, there has been a dramatic increase in the number of bankruptcy filings, both personal and business, since the Act went into effect in October 1979. Many attribute this increase primarily to new provisions of the law which made it easier to file for bankruptcy. Others, however, stress the importance of such other factors that occurred at about the same time as the recession in the economy, the lessening of the stigma attached to declaring bankruptcy, and the increased advertising and publicity by attorneys offering their services to potential bankruptcy clients.

A second development has been the moves of currently solvent corporations to file for reorganization under provisions of the Bankruptcy Reform Act in order to forestall losses that are anticipated as a result of extensive damage claims in product liability lawsuits, or as a result of union contracts that contain compensation provisions that threaten the survivability of the firm.

In June 1981, the Congressional Research Service of the Library of Congress issued a report, "The Bankruptcy Reform Act of 1978 and the United States Economy: A Tentative Look at Some Interrelationships" (81-145-E), by Julius Allen, assisted by Mark Jickling, which provided some preliminary assessments of the impact of the 1978 Act. In September 1981, the same authors prepared a supplementary report, "Business Failure: A Review of the Concept and Its Significance in the American Economy" (81-195-E). This report is designed to update those 1981 reports on the basis of more recent and complete statistics on bankruptcies and business failures, a number of studies and reports on the impact of certain provisions of the Bankruptcy Reform Act, other developments within the last two years, and recent proposed legislation to amend the Act.

This report will not deal with one major issue of controversy that has arisen concerning the act, that of court systems to deal with bankruptcies. The Bankruptcy Reform Act established a new court system with jurisdiction over disputes related to bankruptcy suits. Section 241 (a) of the Act provided for the jurisdiction of both district and bankruptcy courts in bankruptcy cases. This section was struck down by the United States Supreme Court on June 28, 1982, in the Marathon case (Northern Pipeline Construction Co. v. Marathon Pipeline Co., 455 U.S. 1013, 102 S. Ct. 2858 (1982)). This issue, including subsequent legislative action through May 1983, is described in the Congressional Research Service typed report, "Bankruptcy Court Reform: Current Developments," by Meredith McCoy, June 2, 1983, 17 pages.

A second subject outside the scope of this report but frequently mentioned in the financial press is the advisability of investment in securities of firms that have filed for bankruptcy.

Finally, this report does not attempt to assess the factors contributing to bankruptcy in specific industries, such as housing or agriculture.

I. BANKRUPTCY AND BUSINESS FAILURE TRENDS, 1973-1983

The most conspicuous and frequently noted trend of bankruptcies and business failures in the past decade has been their marked increase, particularly since the end of 1979. Table 1 and chart 1 show these trends by quarter, beginning with the first quarter of 1973, for three series: personal bankruptcy filings, business bankruptcy filings, and business failures. 1/ Of these series, personal bankruptcy filings are numerically by far the largest, ranging from 4 to 8 times the number of business bankruptcy filings. 2/ It should be noted, however, that the business failure data of Dun and Bradstreet is much more limited than business bankruptcy filing data, usually involving from one-half to one-fifth as many firms. 3/

As table 1 and chart 1 show, personal bankruptcy filings rose steeply beginning in the last quarter of 1979 until the second quarter of 1981, but have essentially levelled off since then. Thus, since the Bankruptcy Reform Act

1/ Personal and business bankruptcy filings are compiled by the Administrative Office of the United States Courts; business failure data are compiled by Dun and Bradstreet, Inc. Filing means the commencement of a proceeding through the presentation of a petition to the clerk of a U.S. district court. The Administrative Office of the United States Courts also compiles data on bankruptcy cases pending and bankruptcy cases terminated. Bankruptcy cases filed are the most widely used statistics of bankruptcies.

2/ In some cases, probably not many, involving small family or personal businesses, the determination of whether a bankruptcy filing is a business or a personal one may not be entirely consistent.

3/ Dun and Bradstreet data are limited to commercial and industrial failures only, and exclude banks, railroads, real estate, insurance, holding and financial companies, steamship lines, travel agencies, etc. On the other hand, it includes not only bankruptcy filings, but other business discontinuances with known loss to creditors, and other arrangements which may or may not lead to discontinuance, including businesses making voluntary compromise with creditors out of court.

went into effect on October 1, 1979, the largest number of personal bankruptcies per quarter was in the second quarter of 1981 (116,880), followed in rank order by the third quarter of 1981 (114,849), the second quarter of 1982 (114,286) and the third quarter of 1982 (113,613). There has been a steady decline in personal bankruptcy filings from the second quarter of 1982 to the first quarter of 1983, the largest drop occurring in that quarter. The second quarter of 1983 shows a slight increase, but it is still lower than any quarter since the second quarter of 1980, except for the first quarter of 1983. Compared to the pre-1980 levels, personal bankruptcy filings are of course high.

The fluctuations in personal bankruptcy filings (PBFs) beginning with the 2nd quarter of 1980 have been relatively slight compared to the increase in the first six months that the Act was in effect. From the fourth quarter of 1979, when PBFs totalled 67,471 to the second quarter of 1980, when they reached 105,439, the increase in bankruptcies amounted to 56 percent. The difference between the lowest quarter since then (1st quarter 1983) to the highest (2nd quarter 1981) was 12 percent. Before the last quarter of 1979, the highest quarterly level of PBF's occurred in the second quarter of 1975, when they totalled 61,260.

Business bankruptcy filings started rising sharply in the first quarter of 1980, but did not peak until the third quarter of 1982. They have fallen in each of the subsequent three quarters. Business failures continued to rise almost every quarter from the last quarter of 1979 to the first quarter of 1983; there was a slight drop in the second quarter of 1983. It appears likely that business bankruptcy filings, and, probably business failures, are somewhat more closely linked to business cycle trends than are personal bankruptcy filings. The Bureau of Economic Analysis of the U.S. Department of Commerce, for example, includes current liability of business failures as one of its leading (rather than lagging) economic indicators at all stages of the business cycle. Data are published monthly in its publication, Business Conditions Digest.

TABLE 1. Bankruptcy Filings and Business Failures, by Quarter, 1973-1983.

<u>Year</u>	<u>Qtr.</u>	<u>Personal Bankruptcy Filings a/</u>	<u>Business Bankruptcy Filings b/</u>	<u>Business Failures</u>
1973:	1	38,185	4,540	2,399
:	2	41,052	4,523	2,474
:	3	40,322	4,549	2,268
:	4	38,114	4,591	2,204
1974:	1	43,354	5,667	2,563
:	2	46,976	5,940	2,516
:	3	47,813	6,043	2,330
:	4	55,403	7,399	2,506
1975:	1	59,878	8,116	3,188
:	2	61,260	8,572	3,052
:	3	52,425	8,562	2,648
:	4	57,484	9,299	2,544
1976:	1	50,726	8,871	2,718
:	2	50,710	8,472	2,498
:	3	46,458	7,803	2,201
:	4	45,839	8,021	2,211
1977:	1	43,614	8,035	2,215
:	2	46,312	8,317	2,260
:	3	44,445	8,086	1,760
:	4	42,189	7,352	1,684
1978:	1	40,025	7,429	1,729
:	2	45,774	7,651	1,696
:	3	45,297	6,801	1,592
:	4	48,127	7,148	1,602

See following page for continuation of table and all footnotes.

TABLE 1 (continued). Bankruptcy Filings and Business Failures, by Quarter, 1973-1983.

<u>Year</u>	<u>Qtr.</u>	Personal Bankruptcy <u>Filings a/</u>	Business Bankruptcy <u>Filings b/</u>	Business <u>Failures</u>
1979:	1	48,160	7,384	1,919
:	2	55,415	8,144	2,044
:	3	57,865	8,481	1,806
:	4	67,471	9,328	1,795
1980:	1	84,096	12,379	2,331
:	2	105,439	15,901	3,137
:	3	110,673	16,398	3,076
:	4	111,699	15,834	3,198
1981:	1	113,478	17,067	3,454
:	2	116,880	17,034	4,429
:	3	114,849	15,687	4,381
:	4	112,158	16,809	4,530
1982:	1	108,793	21,648	5,705
:	2	114,286	23,581	6,243
:	3	113,613	25,479	6,624
:	4	113,389	24,659	6,774
1983:	1	104,462	24,448	7,633
:	2	108,579	20,939	7,504

a/ Includes non-business joint petitions beginning 4th quarter, 1979.

b/ Includes business joint petitions beginning 4th quarter, 1979.

Sources: Administrative Office of U.S. Courts. Statistical Analysis and Reports Division.

Business failure data from Dun & Bradstreet, Inc.

CHART 1: BANKRUPTCIES AND BUSINESS FAILURES BY QUARTER, 1973-1983

(SHADED AREAS REPRESENT PERIODS OF ECONOMIC RECESSION)

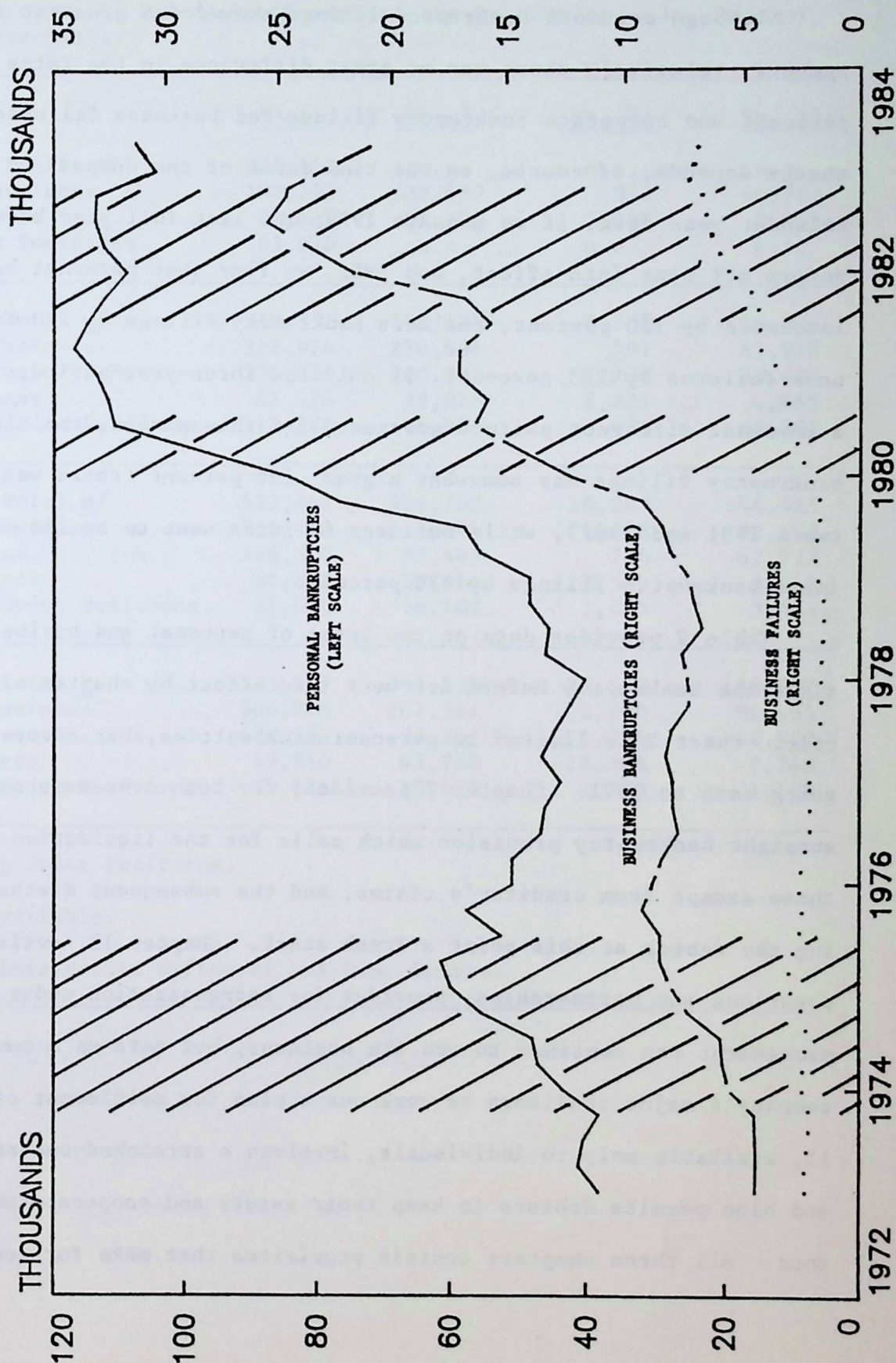


Chart prepared by CRS. See Table 1 for sources of data.

Although personal bankruptcy filings showed the greatest increase in total numbers, relatively there was no great difference in the rates of increase of personal and corporate bankruptcy filings and business failures. The relative change depends, of course, on the time frame of the comparison. Thus, using calendar year data, if we compare 1978, the last full year before the Bankruptcy Reform Act went into effect, and 1982, we find that personal bankruptcy filings increased by 150 percent, business bankruptcy filings by 220 percent, and business failures by 283 percent. If only the three-year period, 1978-81, is used, a somewhat different pattern emerges. For this period, the rise in personal bankruptcy filings was somewhat higher, 156 percent (there was a decline between 1981 and 1982), while business failures went up by 154 percent, and business bankruptcy filings by 130 percent.

Table 2 provides data on the trend of personal and business bankruptcies since the Bankruptcy Reform Act went into effect by chapter of the bankruptcy code. Chart 2 is limited to personal bankruptcies, but covers a longer period, going back to 1971. Chapter 7 provides, for both consumers and businesses, the straight bankruptcy provision which calls for the liquidation of assets beyond those exempt from creditor's claims, and the subsequent discharge of debt, giving the debtor at this point a fresh start. Chapter 11, available only to corporations and partnerships, provides for reorganization under which a firm's management can continue to run the business, but sets up a committee of the company's major creditors to work out a plan for settlement of debts. Chapter 13, available only to individuals, involves a stretched-out repayment plan, and also permits debtors to keep their assets and cooperate with their creditors. All three chapters contain provisions that make for readier access to

TABLE 2. Bankruptcy Cases Filed, by Chapter of the Bankruptcy Code, October 1979-June 1983.

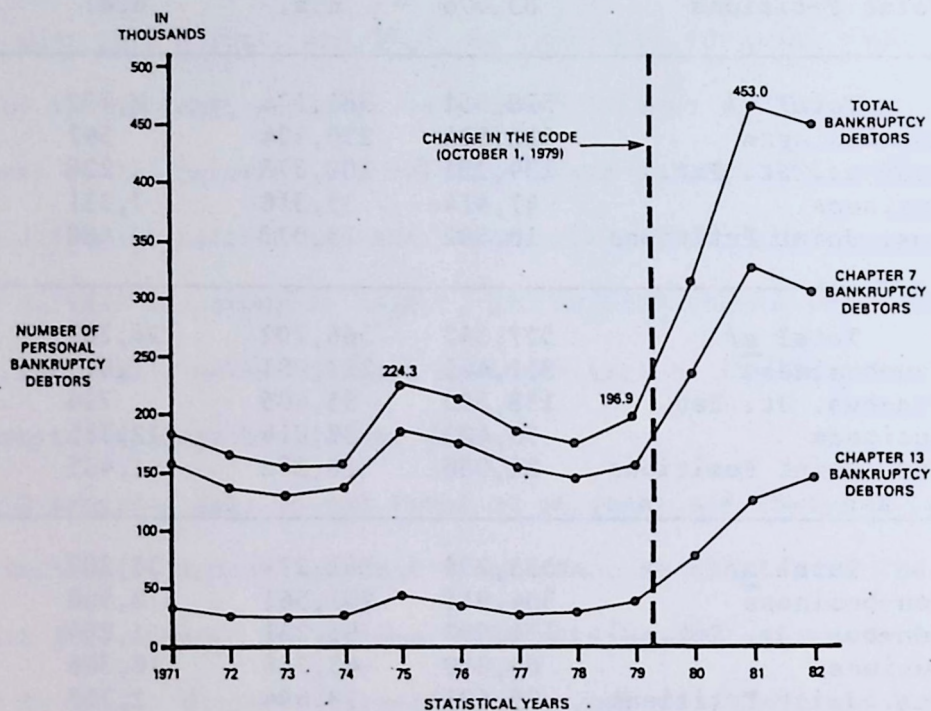
		<u>Total</u>	<u>Ch. 7</u>	<u>Ch. 11</u>	<u>Ch. 13</u>
9 Mos. ending 6/30/80	Total <u>a/</u>	293,443	n.a.	n.a.	n.a.
	Non-business	182,733	137,457	313	44,963
	Business	27,629	21,132	4,002	2,495
	Joint Petitions	83,076	n.a.	n.a.	n.a.
Year ending 6/30/81	Total <u>a/</u>	518,351	381,174	8,752	128,225
	Non-business	312,914	230,404	597	81,913
	Non-bus. Jt. Pet.	139,231	100,375	236	38,620
	Business	47,414	35,318	7,231	4,865
	Bus. Joint Petitions	18,592	15,077	688	2,827
Year ending 6/30/82	Total <u>a/</u>	527,342	366,702	16,207	144,425
	Non-business	311,443	217,081	1,673	92,689
	Non-bus. Jt. Pet.	138,396	95,405	714	42,277
	Business	56,423	38,014	12,385	6,016
	Bus. Joint Petitions	21,080	16,202	1,435	3,443
Year ending 6/30/83	Total <u>a/</u>	535,299	361,274	25,203	148,822
	Non-business	304,916	207,561	2,900	94,455
	Non-bus. Jt. Pet.	134,952	91,261	1,264	42,427
	Business	69,810	43,758	18,306	7,746
	Bus. Joint Petitions	25,621	18,694	2,733	4,194

a/ Including Joint Petitions.

n.a. = not available.

Source: Administrative Office of the U.S. Courts.

CHART 2. Personal Bankruptcy Filings in the United States by Chapter of the Bankruptcy Code, Years Ending June 30, 1971-1982.



Source: Administrative Office of the U.S. Courts [in] U.S. General Accounting Office. Bankruptcy Reform Act of 1978--A Before and After Look. (GAO/GGD-83-54) Washington, 1983. p. 2.

bankruptcy proceedings than was previously available. 4/ There are, however, some offsetting provisions, particularly in business bankruptcies. (See p. 24-25 below.) Chapter 7 filings accounted for from 68 to 75 percent of all personal bankruptcy filings with Chapter 13 accounting for 25 to 31 percent. For businesses, the percentage filing under Chapter 7 was very similar, 65 to 76 percent, with Chapter 11 (available only to corporations) accounting for from 12 to 22 percent and Chapter 13 (for personal unincorporated businesses) accounting for 9 to 13 percent of all business filings.

It was the intent and expectation of Congress that more debtors would seek relief under Chapter 13. As Judge Cecilia Goetz has noted:

The goal which Congress set for itself was to encourage as many debtors as possible to elect repayment plans rather than straight bankruptcy, reserving the latter for those in deep distress. At the same time, Congress wanted to assure those constrained to file for straight bankruptcy that they would emerge with a true 'fresh start,' free from creditor pressure to resume any part of their former debts.... Chapter 13 gives the debtor enormous freedom to restructure and reduce all his obligations, both secured and unsecured, under the shelter of the bankruptcy court. And he does so while remaining in full possession of his property, both exempt and non-exempt. 5/

However, as chart 2 shows, the expectation of Congress that debtors would tend to opt for Chapter 13 repayment plans instead of Chapter 7 straight bankruptcy has not actually occurred. "Chapter 7 is the first choice of most debtors, with Chapter 13 being utilized only where, for one reason or another, the relief under Chapter 7 is inadequate." 6/

There was some increase in the proportion of personal bankruptcy filings utilizing Chapter 13, but still less than half the number resorting to Chapter 7.

4/ For further discussion, see: Allen, Julius. The Bankruptcy Reform Act of 1978. p. 6-9.

5/ Goetz, Cecelia H. Consumer Bankruptcies: Should Ability-to-Pay Condition Bankruptcy Relief? New York Law School Law Review, v. 27, no. 3, 1982. p. 711, 719.

6/ Ibid., p. 725.

Since the significant rise in bankruptcy filings and in reported industrial business failures occurred shortly after the Bankruptcy Reform Act of 1978 went into effect, beginning on October 1, 1979, there is a strong disposition among many analysts to attribute this rise in some measure to provisions of the Act itself. This is borne out by most of the studies cited below.

However, it is patently difficult to determine the significance of the law, compared to other factors, and more particularly of specific provisions of the law, which could be expected to account for the increase. Some general factors not intrinsic to the law, but probably influenced by the passage of the Act, are believed to have contributed to the rise. These would include, for example, the interest among lawyers, as reflected in part by their increased advertising of their bankruptcy law services, the lowering of the stigma attached to bankruptcy, media coverage of bankruptcy as a solution to debt, and the continuing increase in the amount of consumer credit being extended. In addition, as already mentioned on page 1, high interest rates induced by inflation, followed by severe recession, have contributed significantly to the rise in bankruptcies since 1979.

Some consider the provisions of the Bankruptcy Code liberalizing the exemptions from the debtor's estate that are subject to claim by creditors as providing a major incentive for filing for bankruptcy. 7/ Others have disputed this factor, for example William Woodward and Richard Woodward, who, in a recent article, suggest that there is little empirical evidence that would show exemptions to be an incentive to voluntary bankruptcy. 8/ Moreover, whatever

7/ Allen, Julius. The Bankruptcy Reform Act of 1978 and the United States Economy. p. 4-5.

8/ Woodward, William J., and Richard S. Woodward. Exemptions as an Incentive to Voluntary Bankruptcy: An Empirical Study. American Bankruptcy Law Journal, v. 57, Winter 1983. p. 53-74. This article is discussed further below, p. 20-21.

impact this provision may have had is likely to be largely dissipated by another section of the Bankruptcy Reform Act which renders the option of Federal exemptions (generally more generous than State exemptions) inoperative if State legislatures prohibit the application of Federal exemptions in bankruptcy proceedings in their jurisdictions. By the end of 1982, 36 States, nearly three-quarters of all the States, had taken such action. 9/

Further, there are great differences among the States in the exemption levels for particular kinds of property, such as homestead, motor vehicles, household goods and professional tools. Many debtors are unable, because of a lack of sufficient equity in a particular form of property to claim the full amount of exemptions.

While a number of studies attribute the rise in personal bankruptcy filings to specific provisions of the bankruptcy code, in particular, the increase in exemptions, the fact that business bankruptcies have risen proportionately about as much as personal bankruptcies would cast some doubt on such reasoning.

9/ These States are Alabama, Alaska, Arizona, Arkansas, Colorado, Delaware, Florida, Georgia, Idaho, Illinois, Indiana, Iowa, Kansas, Kentucky, Louisiana, Maine, Maryland, Minnesota, Missouri, Montana, Nebraska, Nevada, New Hampshire, New York, North Carolina, North Dakota, Ohio, Oklahoma, Oregon, South Carolina, South Dakota, Tennessee, Utah, Virginia, West Virginia, and Wyoming. Bankruptcy Service, Lawyers Edition. Supplement to Binder 3, April 1983, 22:6. p.53-55.

II. STUDIES RELATING TO THE IMPACT OF THE BANKRUPTCY REFORM ACT ON PERSONAL BANKRUPTCIES

Since the 1981 CRS report on the Bankruptcy Reform Act, referred to on page 1 of this report, there have been a number of studies that have attempted to assess, directly or indirectly, the impact of the Bankruptcy Reform Act or certain of its provisions on the American economy. While all of the reports point to or imply some impact of the Act, the range of opinion as to the extent of this impact is wide. Seven reports are reviewed.

1. The first of these reports, which has received wide publicity, was the outcome of a study conducted by the Credit Research Center at Purdue University under the direction of Robert W. Johnson which was financed by firms in the consumer credit industry. ^{10/} Its focus was not directly on the impact of the Bankruptcy Reform Act itself, but was, rather, an attempt to determine to what extent individuals who had filed for personal bankruptcy under Chapter 7 of the Act had the ability to pay off their debts out of future income. Its conclusion that many individuals who filed for Chapter 7 bankruptcy would be able to pay off all or part of their nonmortgage debts out of future income directly suggested that such individuals were being unduly favored in being allowed to file for bankruptcy under Chapter 7 rather than filing under Chapter 13 where

^{10/} Consumers' Right to Bankruptcy. West Lafayette, Indiana. Krannert Graduate School of Management, Purdue University, 1982. 137 p.

payment of all or part of debts out of future income is a part of the bankruptcy plan. 11/

The study was based primarily on interviews of individuals involved in 1,199 Chapter 7 bankruptcy petitions in ten States, with approximately 120 bankruptcy petitioners in each State. States selected were those with two or more judicial districts, five of which (Georgia, Illinois, Louisiana, Ohio and Virginia) had lower exempt property standards than the Federal Bankruptcy Code and five (California, New York, Pennsylvania, Texas, and Wisconsin) with exemption standards at least as high as those provided by the Bankruptcy Code. The two groups are referred to as low-exemption and high-exemption States.

The overall conclusion derived from this set of interviews was that, depending on the assumptions made, "15 percent to 30 percent of bankrupt debtors probably could repay all of their nonmortgage debts out of their future income, while as many as 37.4 percent of bankrupt debtors probably could repay at least half their debts out of future income... Because consumers typically borrow against future income rather than assets, only five percent of the respondents could repay their debts by liquidating assets, and half of these would not have been able to repay their debts from future income." 12/

Robert W. Johnson, director of the study, reaches the following additional conclusions in a final chapter on public policy issues:

11/ Although not reflected in the report's title, it is apparent that the impact of the Bankruptcy Code on the Nation's economy was a major concern of the authors of the report. Note, for example, the title of the statement on p. 106 of the report, "The Economic Impact of the Bankruptcy Code." This statement was attached to personal interview questionnaires sent out by Opinion Research Corporation, a subsidiary of Arthur D. Little, Inc., which cooperated with the Credit Research Center in preparation of this report.

12/ Ibid., p. 72.

(1) First, the amount of potentially recoverable Chapter 7 debts has been estimated to be \$1.1 billion annually, assuming a five-year payback. These debts would be recoverable from anticipated future income after meeting basic living expenses and actual housing costs. The estimates vary with the payout period and the size of any cushion provided over and above basic living expenses, with the overall range from \$0.6 billion to \$1.1 billion annually.

(2) Second, 50 percent to 60 percent of Chapter 7 debtors would be unaffected by the change being considered by the U.S. Congress. ^{13/} These consumers are primarily low-income consumers without adequate income above basic living expenses and housing costs to repay a reasonable portion of their debts. In contrast, about 70 percent of the potentially recoverable debts was owed by those debtors who could have repaid all of their nonmortgage debts over a period of no more than five years. ^{14/}

This study has been widely cited by proponents of new legislation that would permit the courts to take into account future income as a source for repayment of debts in Chapter 7 proceedings. ^{15/} The study has been criticized by consumer groups, such as the National Consumers League, Consumer Federation of America, Consumers Union, and others, on various grounds including the size and composition of the sample, the nature of the interviews, and alleged bias as a result of industry sponsorship.

2. A May 1982 Federal Reserve Bulletin survey of developments in the mortgage and consumer credit markets, argued that:

Most of the additional increase [in personal bankruptcies since the end of 1979] appears to be traceable to sweeping changes in the National Bankruptcy Act effective in late 1979 that made bankruptcy less onerous for debtors, particularly its provisions for broader protection of assets from liquidation than generally had

^{13/} See p.31-32 for description of the changes which would limit the extent to which debtors with ability to repay debts out of future income could file for bankruptcy under Chapter 7.

^{14/} Consumers Right to Bankruptcy, p. 99.

^{15/} Under present law, the discharge of the debtor and settlement with creditors under Chapter 7 proceedings are determined by the assets of the debtor above specific exemption levels. By contrast, Chapter 13 proceedings provide a rehabilitation alternative to the liquidation plan of Chapter 7 for debtors with regular incomes.

been available under previously applicable state regulation. The uptrend in bankruptcies slowed considerably in 1981, however, suggesting that the legal changes may have led to a one-time adjustment in the level of bankruptcies rather than a pattern of continuous sharp year-to-year increases. ^{16/} Moreover, some states have exercised the right under the Federal law to reimpose their own set of property exemptions, which most likely has helped to retard the advance. Nevertheless, the earlier surge in bankruptcies, together with concern over possible future increases, has prompted more conservative lending practices, such as the growing emphasis on securing loans by real estate. ^{17/}

3. The study of Charlie Carter, published in January 1982, reaches conclusions similar to those of the Federal Reserve Bulletin article just cited. ^{18/} Specifically, it concludes: (1) the 1978 Bankruptcy Act added significantly to the annual volume of personal bankruptcies filed in the United States in general and in the Southeast. This conclusion is reached regardless of the assumption one makes regarding the relative severity of the 1980 recession vis-a-vis its predecessors. (2) The relative influence of the new law was less important in the Southeast than for the U.S. as a whole. (3) The new code's influence became more pronounced the longer it was in effect. Although the new code was responsible for almost 20 percent of the increase in personal cases filed in 1979-80 in the Southeast and about 46 percent of the increased cases filed nationally during the same period, it was responsible for over 64 percent of the cases filed in the Southeast and 72 percent of the cases filed nationally in the year ending June 30, 1981.

The third conclusion does not appear to be borne out by statistics on personal bankruptcies since fiscal year 1981. As noted above (p. 3-4) personal bankrupt-

^{16/} See statistics in table 1 and chart 1 that corroborate this statement.

^{17/} Luckett, Charles. Recent Developments in the Mortgage and Consumer Credit Markets. Federal Reserve Bulletin, v. 68, May 1982. p. 289-90.

^{18/} Carter, Charlie. The Surge in Bankruptcies: Is the New Law Responsible? Federal Reserve Bank of Atlanta Economic Review, January 1982. p. 20-30.

cies were lower in calendar year 1982 than in calendar year 1981 and in the first quarter of 1983 were lower than in any quarter since the first quarter of 1980.

4. Based on data through June 30, 1981, and using a regression model he developed, Kowalewski 19/ comes to the conclusion that the Bankruptcy Reform Act is not as significant a factor in the rise of personal bankruptcies as many others have contended. 20/ Kowalewski concludes that the Bankruptcy Reform Act may be the cause of about 30 percent of the increase in personal bankruptcy filings, with 70 percent being the result of other factors, including inadequacies of personal income, deficiencies in the size and composition of assets of consumers, and high interest rates. Another, but probably minor, one-time factor may have been the Consumer Credit Restraint Program of the Board of Governors of the Federal Reserve System, effective from March 14, 1980, to July 3, 1980, which reduced the supply of consumer credit during those months and, thereby, may have forced some financially pinched consumers to file for bankruptcy.

Kowalewski concludes that the new Federal exemption levels in the Bankruptcy Reform Act, should, in themselves, be expected to have increased the level of personal bankruptcy filings (PBFs). He maintains:

...Under the old bankruptcy law, only state exemption levels were available, and these were infrequently and imperfectly adjusted for inflation. Hence, real exemption levels fell over time, possibly suppressing the number of PBFs until the new code took effect. Much of the unexplained increase in PBFs may be just a natural reaction to an inflation-adjusted new law. Assuming lawmakers expected PBFs to increase for this reason, the relevant question to answer is how much of the increase in PBFs is an undesired result of the new code? 21/

19/ Kowalewski, K.J. Personal Bankruptcy: Theory and Evidence. Federal Reserve Bank of Cleveland. Economic Review, Spring 1982. p. 1-29.

20/ See, for example, the studies of Charlie Carter and Charles Luckett cited above, p. 16-17.

21/ Kowalewski, K.J. Personal Bankruptcy, p. 28.

Kowalewski concludes: "The argument that the new code has a large impact on PBFs would be supported by future PBFs remaining at very high rates. Arguments for changing the new code would be severely undercut if PBFs declined to rates found in the old bankruptcy law period." 22/

In fact, as seen in the data presented above, pages 4-8, the trend through the second quarter of 1983 seems to lie between the two extremes suggested by Kowalewski. Rates have come down from the peak in the second quarter of 1981 but are still far above the rates that prevailed before 1979.

5. Philip Shuchman, professor of law at Rutgers School of Law, Newark, N.J., made a study of 753 personal bankruptcy filings in 1979-81 in eight States (Arizona, California, Georgia, Maryland, Massachusetts, Missouri, Pennsylvania, and Virginia) and the District of Columbia. 23/ It was a sequel to an earlier study limited to the State of Connecticut. 24/

Shuchman considers his major finding to be that "most of the debtors in personal bankruptcy under Chapter 7 are poor or near-poor by the usual Bureau of Labor Statistics and Census Bureau Standards." Their real incomes decreased over the three years, 1978-1980.

Further, in 1980, the last year for which there is a large enough number, one-third (33%) of the debtors reported total incomes below the poverty level of \$8,418. Sixty-two percent (62%) reported total incomes which were less than the BLS "lower living budget" of \$14,044. Only sixteen percent (16%) of the debtors

22/ Ibid., p. 28.

23/ Shuchman, Philip. The Average Bankrupt: A Description and Analysis of 753 Personal Bankruptcy Filings in Nine States. Commercial Law Journal, v. 88, June-July 1983. p. 288-307.

24/ Shuchman, Philip and Thomas Rohrer. Personal Bankruptcy Data for Opt-Out Hearings and Other Purposes. American Bankruptcy Law Journal, v. 56, Winter 1982. p. 1.

reached the national median family income of \$21,020. In none of the three years, from 1978 through 1980, did more than 3% of the debtors report total incomes larger than the BLS "higher living budget," which was \$34,409 in 1980.

The debtors' latest average annual income was \$13,600, counting only those debtors reporting income. Were those without any income included, the average would decline to \$13,177. Their average total of all reported debt (except for mortgages) was \$17,432, which is about 136% of their average total incomes computed for the two years called for in the Statement of Affairs. 25/

The Shuchman study and that of the Credit Research Center of Purdue University, described above, although difficult to compare in key respects, nevertheless offer interesting contrasting perspectives. Similar data were used in the two studies, both dealing with Section 7 bankruptcy filings. The Purdue study was based on 1,199 interviews of individuals involved in Chapter 7 bankruptcy, the Shuchman study on 753 bankruptcy schedules filed in the courts. The Purdue study took in all or parts of ten States, the Shuchman study seven States and the District of Columbia. Three States (Georgia, Pennsylvania, and Virginia) were included in both studies. The focus of the studies differed substantially: the Purdue study attempted to assess the ability of individuals who had filed for bankruptcy to pay off their debts out of future income, a subject not explicitly referred to in the Shuchman study. The Shuchman study provided more detail on the nature of individual indebtedness and the sources of credit. The Purdue study stressed the substantial fraction of individual bankruptcy filers who would be in a position to pay off all or major parts of their debt from future income. The Shuchman study, by contrast, stressed the low income of most filers for

25/ Shuchman, Philip. The Average Bankrupt. p. 306. The Statement of Affairs is part of the bankruptcy schedules filed in the courts.

bankruptcy and, by implication, the need to retain in the bankruptcy proceedings the right of such filers to get a fresh start, without the overhang of burdensome debt obligations for extended periods, from three to five years.

6. William J. Woodward and Richard S. Woodward have raised considerable doubt as to the allowable level of exemptions as a significant factor in the decision of individuals to file for personal bankruptcy. 26/ Their basic conclusions may be cited:

For the years tested [fiscal years 1979 and 1980], this study establishes only that there is no statistically significant relationship between state bankruptcy rates and the incentive to bankruptcy, as we defined it, found in the state's applicable bankruptcy exemption provisions. At minimum, the results suggest that the dynamics of the debtor's bankruptcy decision are far more complex than the exemption-incentive notion recognizes; the results also underscore the oversimplification implicit in the incentive notion. In addition, the results also show that the simple reduction in present [U.S.] Code exemption levels probably will not result in a significant reduction in the number of voluntary bankruptcy filings. 27/

Among the reasons that the Woodwards give as an explanation for the relative lack of importance of exemptions in decisions to seek bankruptcy are the following: (1) there are strong reasons for seeking bankruptcy, such as the need to gain immediate relief from credit collection efforts, and the debtor's incurrence of large medical expenses, regardless of the exemption level that comes with the choice of bankruptcy; (2) it appears likely that most consumer debtors decide on bankruptcy before they have any awareness of the significance of exemptions at all; (3) the value of an exemption to an individual depends not only on the size of the exemption provisions but also on whether the debtor happens to own the specified property; the Woodwards found no way to determine

26/ Woodward, William J., Jr., and Richard S. Woodward. Exemptions as an Incentive to Voluntary Bankruptcy: an Empirical Study. American Bankruptcy Law Journal, v. 57, Winter 1983. p. 53-74.

27/ Ibid., p. 66.

with any accuracy how many persons choosing bankruptcy in the various States had the "right" kinds and amounts of property to make particular exemption levels a determining factor in their decisions. 28/

7. Most recent is a report of the General Accounting Office based on a two-year study of personal bankruptcies filed before and after October 1, 1979. 29/

Its primary sources were a random sample of seven percent of personal bankruptcy cases in five Federal bankruptcy court districts (southern and eastern New York, southern Ohio, eastern Kentucky, and central California) during two sample periods: October 1978 to March 1979 (before the Act) and April to September 1980 (after the Act); and, a questionnaire which was mailed to a randomly-selected nationwide sample of individuals who filed Chapter 7 and Chapter 13 personal bankruptcies during October 1981, to determine the factors that led to personal bankruptcy and obtain additional information on the personal characteristics of bankruptcy debtors.

Probably the principal conclusion of the report is the relatively small impact, according to its analysis, that the Bankruptcy Reform Act is believed to have contributed to the number of personal bankruptcy filings; the report concluded that in fiscal year 1982 not more than six percent of total adjusted filings were attributable to the Act.

The report states this conclusion as follows:

28/ Ibid., p. 66-68.

29/ U.S. General Accounting Office. Bankruptcy Reform Act of 1978--A Before and After Look. Report to the Chairman, Committee on the Judiciary, House of Representatives. (GAO/GGD-83-54). Washington, July 20, 1983. 106 p. A limited study of the financial status and characteristics of five bankruptcy petitioners was undertaken by the General Accounting Office in 1982 under the title, "A Profile of Selected Personal Bankruptcy Cases." (GAO/GGD-83-16). November 4, 1982. 16 p.

Social and economic factors have impacted upon the number of bankruptcy filings which have increased substantially since the revision of the Bankruptcy Code. Our regression analysis, exclusive of unquantifiable variables such as the influence of attorney advertising and the amount of social stigma associated with bankruptcy, showed that in fiscal year 1982 the implementation of the code may have contributed no more than 6 percent of the total adjusted filings. However, it is possible that the actual impact of the code could have been less if the impact of the unquantifiable factors could have been estimated. 30/

The social and economic factors specified by the report as being the most significant ones for both chapters 7 and 13 debtors were increases in the cost of living, too many debts, easy credit availability, unemployment, unusual medical bills and, especially, creditors' threats or notifications of legal action. 31/

Finally, the study indicated that although it found that there was similarity among some debtors filing under chapter 7 and others under chapter 13 with respect to income, assets, and debt characteristics, it could not conclusively affirm that debtors could have repaid their debts out of future income.

In order to make such a conclusion, detailed information on chapter 7 debtor living expenses, family size, and other characteristics would be needed; however, such information is not currently reported in bankruptcy court records. 32/

30/ Ibid., p. 20.

31/ Ibid.

32/ Ibid., p. 59.

III. DEVELOPMENTS IN CORPORATE BANKRUPTCY

The increase in personal bankruptcies that followed the passage of the Bankruptcy Reform Act has probably received greater attention than the increase in corporate bankruptcy, in part due to the sizeable efforts of the consumer credit and banking industries to persuade the Congress to enact legislation that would place more limits on the ability of individuals to file for bankruptcy. However, as was shown in Chapter 1, increases in corporate bankruptcy and reorganization have been proportionately as great as personal bankruptcy filings. A November 1982 report of the National Journal concludes:

It is impossible to determine to what degree the 1978 reforms have encouraged bankruptcies. The growing number of failing companies, of which reorganization cases account for about 20 percent, could be attributed to the high inflation of the late 1970s and the current recession. Prior to 1978, more companies in trouble liquidated than reorganized. 33/

A recent paper by Michelle J. White of New York University Graduate School of Business Administration argues:

From an economic standpoint, the most important changes instituted under the new Bankruptcy Code had the effect of making it more difficult to reorganize firms in bankruptcy... The new Code preserves reorganization as an option for failing firms, but makes it more difficult to use the procedure and introduces some new alternatives. 34/

Specific ways in which the new Bankruptcy Code makes it more difficult to reorganize in bankruptcy cited by Michelle White are the following:

33/ Cater, Morrow. Manville Bankruptcy Case May Prompt Congress to Close 'Loophole' in Law. National Journal, November 27, 1982. p. 2029.

34/ White, Michelle J. Bankruptcy Costs and the New Bankruptcy Code. Journal of Finance, v. 38, May 1983. p. 477-478.

For example, the voting requirements for adopting a reorganization plan were stiffened by changing the margin from a simple majority to two-thirds in amount of each class voting in favor and by requiring that secured as well as unsecured creditors' classes approve the plan if their claims are adversely affected. Also, managers have lost the exclusive right to propose the plan. This means that creditors can propose their own plans and are no longer faced with a take-it-or-leave-it choice between management's plan or piecemeal liquidation. Another new alternative is that if no plan is agreeable to all parties, the firm can continue operating while a buyer is sought for all or part of it as a going concern, thus often obtaining a better price than if its assets were sold piecemeal. Finally, the new Code removes the restriction that firms reorganizing must continue in the same form. Any or all of the firm's operations can be shut down and/or sold. 35/

Whether or not the new Code has been responsible for greater or fewer corporate reorganizations, it seems clear that corporations are attempting to utilize the corporate reorganization provisions of the new Code in new ways that are receiving considerable publicity. Corporations that are currently solvent have filed for reorganization to forestall losses they believed would result in business failure, for a number of reasons, including the effect of massive damage claims resulting from asbestos-related diseases, the impact of the collective bargaining agreement with a labor union, as well as anticipated losses in retail trade.

A. Chapter 11 Filings by Asbestos Companies

Three companies that are or have been producers of asbestos filed for reorganization under Chapter 11 of the Federal Bankruptcy Code in 1982 because of pending and anticipated lawsuits against them resulting from asbestos-related diseases. They are: UNR Industries, which filed for reorganization on July 29, 1982; Manville Corporation, parent company of Johns-Manville Corporation, which filed for reorganization on August 26, 1982, for itself and 20 of its domestic

35/ Ibid., p. 479-480.

subsidiaries; and Amatex Corporation, which filed for reorganization on November 2, 1982.

Manville alone had more than 16,500 asbestos health lawsuits pending at the time it filed for reorganization, with 500 new claims being added monthly during 1982. A study commissioned by Manville estimated the minimum number of additional future lawsuits against Manville to be 30,000. Thus, as a recent law review article noted,

...of the approximately 50,000 present and projected claims on which Manville blames its filing, almost 30,000 have not yet been brought and will be filed (if at all) by unknown plaintiffs, while nearly all 50,000 are contingent and unliquidated. 36/

The claims against Manville Corporation were of two kinds: as a supplier of asbestos to other businesses, and as the employer of individual workers.

One article reported:

The discounted cost of all expected claims present and future is by conservative estimates something over \$2 billion. The net worth of the company, asbestos claims to one side, is just over \$1 billion. 37/

The Manville case is striking in that Manville is attempting to base its filing for reorganization to a major extent on indeterminate contingent liabilities. As the Harvard Law Review note cited above states:

The Manville filing presents a stark contrast to the traditional reorganization case, in which the debtor knows the identities of its creditors and the amount of its debts. In such cases, the debtor seeks the aid of the court only in restructuring its finances and satisfying its existing creditors to the greatest extent possible. The most extraordinary aspects of the Manville case are that the majority of Manville's creditors are unknown and that the majority of the debts on which Manville bases its claim of prospective insolvency are contingent and unliquidated. Manville thus appears to

36/ The Manville Bankruptcy: Treating Mass Tort Claims in Chapter 11 Proceedings. Harvard Law Review, v. 96, March 1983. p. 1122.

37/ Epstein, Richard A. Manville: The Bankruptcy of Product Liability Law. Regulation, v. 6, September-October 1982. p. 14.

be attempting to use the bankruptcy power largely as a tool to limit the aggregate size of its current and future liabilities. If successful, Manville's strategy will have a profound effect on all asbestos-related tort litigation. 38/

Manville's reorganization under Chapter 11 is still in process. The court has given Manville seven extensions of its deadline to submit a reorganization plan, with October 17, 1983, being the current deadline. Drawn out litigation appears likely.

Many legal questions arise from these asbestos company tactics. Can the bankruptcy system appropriately be used by an otherwise solvent company facing massive liability claims? Can courts discharge today a company's liability to workers who may not become affected by asbestos-related diseases for many years? Can judges decide the amount to be set aside to meet future claims before such claims are filed? Can a court set a value on the total debts of a company to injured workers, present and future? Can a bankruptcy court limit itself to estimating the corporation's total liability and establishing a compensation fund for the plaintiffs, while allowing the plaintiffs to pursue their claims in the State and Federal courts in which such claims were originally filed, and then return to the bankruptcy court to execute their judgments on a pro rata basis against the compensation fund? Can the Bankruptcy Court cut off the rights of future claimants?

Thus far, the most definite legal answer to some of these questions was given by Judge William T. Hart in the United States District Court for the Northern District of Illinois on March 25, 1983. 39/ UNR Industries had asked the court to appoint a legal representative to represent interests of individuals who

38/ The Manville Bankruptcy. p. 1122.

39/ In re: UNR Industries, Inc. Bankruptcy Nos. 82 B 9841 - 82 B 9851. 29 Bankruptcy Reporter 741 (D.C. 1983).

might have been exposed to asbestos and might file a claim against UNR for injuries resulting therefrom. Judge Hart rejected the request, stating, "There simply is no authority in the statute or the Constitution for this Court to grant the debtors the relief they seek." 40/

He pointed out that if the petition of the asbestos company prevailed,

...any manufacturer of a potentially dangerous product [such as benzene or diethyl stilbestrol (DES)] would be able to file a petition under Title 11. . .asking that a legal representative be appointed to protect the interests and negotiate a plan (including the discharge of all future claims) for those who some day might be injured by a product placed into the stream of commerce by the manufacturer debtor. Bankruptcy courts would be forced to speculate as to the future dangerousness of and damages caused by any product which some day after a discharge in bankruptcy might be found to harm someone.... No individual could represent such a large group [of people who do not yet know they have any disease and may not experience any health problem for the next forty years] with conflicting positions on such various and complex issues.... It would be impossible for one legal representative to represent adequately the claims of tens of thousands of future claimants. 41/

Judge Hart argued that the solution to the problem of dealing with the claims resulting from health damages in terms of fairness both to the claimants and to the defending corporations needs to be addressed by the Congress and not by the courts. He said:

...the Court is aware that there are proposals before Congress to create solutions for these problems, both for the companies and the present and future claimants. That is the place a solution must be found. 42/

Clearly, the issue is as yet far from being resolved.

B. Chapter 11 Filings because of Wage Costs

On April 22, 1983, Wilson Foods Corporation filed for Chapter 11 reorganization in order to stave off losses resulting, it claimed, from a labor agreement

40 Ibid., p. 748.

41/ Ibid., p. 747.

42/ Ibid., p. 748.

with the United Food and Commercial Workers International Union. Under the protection of the court under the Bankruptcy Code, Wilson repudiated its labor agreement and cut wages 40 to 50 percent. One law professor, Frank R. Kennedy of the University of Michigan Law School, argued that "Wilson has taken the law into its own hands. It was highhanded. It was rash. And it looks reckless." 43/ Others feels that, in view of the losses the company was sustaining and the drop in its net worth, filing for reorganization under Chapter 11 was the only realistic way of staving off collapse.

The outcome of the case is still to be decided. According to a May 1983 Wall Street Journal report:

Some experts are betting that while Wilson may be found guilty of an unfair labor practice, the courts ultimately will grant the company what it wants, the right to negotiate a new and cheaper labor contract. That could encourage imitators. 'The easier the courts make it for Wilson, the more other companies will be encouraged,' says Vern Countryman, a professor and bankruptcy expert at Harvard Law School. 44/

The Wilson Foods case is not wholly without precedent. Bildisco, a partnership selling building supplies in New Jersey, filed for bankruptcy under Chapter 11 in 1980, and a year later sought court approval to reject terms of a collective bargaining agreement with Teamsters Local 408. This rejection was approved by Bankruptcy Judge Amel Stark and in essence upheld in 1982 by a three-judge panel of the U.S. Court of Appeals in Philadelphia. 45/

On September 24, 1983, Continental Airlines Corporation filed for bankruptcy under Chapter 11, citing excessive labor costs. It stated that it would pare its labor forces by two-thirds and cut wage rates for remaining

43/ Sorenson, Laurel. Chapter 11 Filing by Wilson Foods Roils Workers' Lives, Tests Law. Wall Street Journal, May 23, 1983. p. 37.

44/ Ibid., p. 37.

45/ For further details, see: Business Week, July 26, 1982. p. 24-25.

workers. Two days later the chairman of Eastern Airlines, Frank Borman, in an appeal to workers to accept wage cuts, suggested that a Chapter 11 filing might be necessary if wage cuts were not accepted.

C. Other Large Corporate Bankruptcies

Many other bankruptcy filings for reorganization under Chapter 11 are, of course, less novel in their rationale. The following are among the largest and most prominent firms whose Chapter 11 reorganizations were in the bankruptcy courts as of the beginning of 1983: (1) Wickes, the Nation's largest retailer of lumber and building material, with net sales of nearly \$4 billion in fiscal year 1982; (2) Itel, a major container operations firm with assets of \$1.2 billion at the end of 1982; (3) Nucorp Energy, Inc., an energy supplier with assets of \$0.8 billion in 1982; (4) Braniff International, an air transportation firm with operating revenues of \$1.2 billion in 1981; (5) Seatrain Lines, Inc., a shipping conglomerate with operating revenues of \$1.3 billion in fiscal year 1980; and (6) Revere Copper and Brass, Inc., one of the largest firms in the nonferrous metal fabricating industry with total assets of nearly \$0.5 billion at the end of 1981.

Braniff's reorganization was approved by Federal Bankruptcy Judge John Flowers in Fort Worth, Texas, on September 1983. Under the reorganization plan, Hyatt Corporation assumes control of Braniff's operations. Flights are expected to resume in 1984.

The filing for bankruptcy by the pioneer computer firm, Osborne Computer Corporation, on September 14, 1983, in New York City, is believed by some analysts to be a prelude to further computer company failures in the near future.

IV. LEGISLATIVE INITIATIVES ON BANKRUPTCY ISSUES

A major focus of legislative proposals to amend the Bankruptcy Reform Act has been on means of curbing the sharp increase in personal bankruptcy filings that has occurred since the Act went into effect on October 1, 1979. One such proposal has been to limit the debtor's recourse to Chapter 7, the straight bankruptcy proviso, if he has the ability to repay his debts out of anticipated future income. ^{46/} This is a step that has been strongly endorsed by most firms and individuals in the credit industry and some others who believe that such a step would lead to the legitimate repayment of substantial amounts of debt, making write-off of such amounts unnecessary, and thereby lessening the burdens on other debtors. It is opposed by consumer groups and many bankruptcy lawyers and judges who maintain that it is premature to make major changes in the bankruptcy code and that such changes would weaken the principle of a justifiable fresh start for heavily burdened debtors. Some of the legislative proposals understandably take a middle course between these polar positions.

The major current legislative move to deal with this issue is the Omnibus Bankruptcy Improvements Act of 1983 (S. 445, 98th Congress), originally introduced by Senator Robert Dole, which passed the Senate on April 27, 1983, and was referred on May 5, 1983, to the House Committee on the Judiciary. As originally introduced, S. 445 would have incorporated a "future income"

^{46/} Such a proposal was made by Andrew Brimmer in testimony before the Senate Committee on the Judiciary on April 3, 1981 (see CRS Report 81-145E), and, by implication, in the Credit Research Center's Consumer Bankruptcy Study cited above, p. 14-16.

threshold test in the law. "Under this test, the courts would have systematically evaluated the ability of debtors to pay a reasonable portion of debts out of future income." 47/

This was deleted, however, and two alternative provisions were submitted as a compromise between the "future income" test and the existing law. First, under Subtitle A, Section 203, of the Senate bill, when a person files for bankruptcy under Chapter 7, the trustee appointed by the court to administer his estate is required to counsel the debtor as to the options available to him under the bankruptcy code. Such counselling is intended to inform but not to force a debtor into a particular choice. Second, a provision [Subtitle A, Section 202(c)] was added to authorize a judge on his own motion to dismiss a case where the granting of Chapter 7 relief would represent a substantial abuse of that chapter. The judge would have to support his decision in writing and give the debtor the chance to respond before making a final decision. A decision denying bankruptcy could be appealed by the debtor to an appellate court. Creditors could not participate in this process except by invitation of the judge.

Similar to S. 445 as originally introduced is H.R. 1800 sponsored by Representative Mike Synar. It is pending in the House Committee on the Judiciary. Representative Rodino, the chairman, has indicated that any action on the consumer credit bill should wait until the bills dealing with the bankruptcy court system are resolved.

On February 1, 1983, Senator Howard Metzenbaum introduced S. 333 in the Senate and Representative Peter Rodino introduced H.R. 1147 in the House of Representatives. These are companion bills to deal with flagrant abuses that

47/ 98th Congress, 1st Session. Senate Report No. 98-65. p. 3-4.

have occurred in personal bankruptcy filings, without adopting a future income provision per se. As Senator Metzenbaum stated upon introducing S. 333:

Our bill is intended to correct these abuses [by debtors of protections afforded them by the bankruptcy laws] without removing the protections needed by deserving debtors who find themselves in serious financial difficulty not of their own making and who need a 'fresh start' free from past economic misfortunes. 48/

These bills of Senator Metzenbaum and Representative Rodino would, among other provisions: (1) set a total exemption limit of \$4,000 on personal and household items, of which each is valued at under \$200; (2) require debtors in a joint bankruptcy filing to choose either State or Federal exemptions (under the present law, it has happened that both State and Federal exemptions have been used by two persons jointly filing for bankruptcy); (3) make nondischargeable any debts aggregating more than \$500 incurred within 45 days of filing for bankruptcy.

H.R. 1085, introduced by Representative George Hansen on January 31, 1983, and H.R. 1169, introduced by Representative Marilyn Bouquard on February 2, 1983, would both establish an eligibility test for Chapter 7 bankruptcy relief that would be based on the individual petitioner's ability to pay a reasonable portion of his debts out of anticipated future income. This is in line with S. 445 as originally introduced and is strongly supported by the credit industry.

Thus far, apparently, no legislation has been introduced specifically to curb the innovative uses of Chapter 11 reorganization petitions to which several corporations have resorted (see p. 24-30 above).

However, the issue of protection for victims of occupational diseases, which has been aggravated by the bankruptcy filings of the three asbestos

48/ Congressional Record (daily edition), February 1, 1983. p. S.798.

companies mentioned above (p. 26-27), is being addressed in the Congress on other fronts. For example, Congressman George Miller of California on May 26, 1983, introduced a bill, H.R. 3175, the Occupational Disease Compensation Act of 1983, which is designed to establish a fair system for providing adequate benefits on a timely basis to occupationally disabled Americans and their survivors. It was referred to the House Committee on Education and Labor. Hearings were held by that Committee's Subcommittee on Labor Standards in June and July 1983.

Further judicial review and interpretation appear likely to precede serious legislative consideration of amendments to Chapter 11 of the Bankruptcy Code.

As noted at the outset of this paper, legislation dealing with the structure of the bankruptcy courts lies outside the scope of this report.

jpc

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